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In The

Supreme Court of the United States

October Term, 1996

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO. and MARCO SEATTLE, INC.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF AMICUS CURIAE OF NATIONAL ASSOCIATION OF MANUFACTURERS AND RAYCHEM CORPORATION IN SUPPORT OF RESPONDENTS

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STATEMENT OF INTEREST

• The National Association of Manufacturers

The National Association of Manufacturers (the "NAM") is the nation's oldest and largest broad-based industrial trade association. Its more than 14,000 member companies and subsidiaries, including 10,000 small manufacturers, employ approximately eighty-five percent of all manufacturing workers and produce over eighty percent of the nation's manufactured goods. More than 158,000 additional businesses are affiliated with the NAM through its Associations council and National Industrial Council.

• Raychem Corporation

Raychem Corporation is a technology based manufacturing company located in Menlo Park, California. Raychem is the defendant in the case entitled *All Alaskan Seafoods, et al. v. Raychem Corporation, W. D. Wash., case no. C 95-351R,* in which a vessel owner seeks economic damages associated with the loss of its vessel, the PV/ ALL ALASKAN, when it burned. Raychem manufactures heating cable products that are wrapped around pipes and covered with insulation to keep the pipes from freezing. Its heating cable product was installed on P/V ALL ALASKAN during a conversion of the vessel into a fish processor, and is alleged to have caused the fire. One of its opponents in this lawsuit, All Alaskan Seafoods, Inc., has filed an amicus brief supporting the arguments of Petitioner.

SUMMARY OF ARGUMENT

The Ninth Circuit's approach in defining the "product," for purposes of the economic loss rule, as the "object" of the plaintiff's bargain finds its support in the fundamental premises of this Court's *East River* decision and the decisions of virtually every court to address the issue. The "object" or "benefit" of the bargain approach is the only principled way to differentiate economic losses, as that term is used in *East River*, from tortious injuries. The Ninth Circuit's rule is fair and accounts for the ability of parties to commercial transactions to allocate the risk of economic losses among them. The Ninth Circuit's decision protects the ability of upstream commercial manufacturers to make meaningful contracts limiting or disclaiming their liability, and to avoid exposure to unlimited economic losses in tort. The rules of law proposed by the Petitioner ignore the rationale of *East River* and would unravel the agreements regarding risk allocations throughout the supply chain. None of the proposed definitions of "product" are reconciled with *East River's* conclusion that tort principles are weak when a product fails or harms itself. The proposed definitions of "product" are arbitrary and incapable of application across a broad range of circumstances in any principled way. In some circumstances, the proposed definitions abrogate the economic loss rule altogether.

ARGUMENT

I. THE NINTH CIRCUIT PROPERLY APPLIED THE "BENEFIT OF THE BARGAIN" ANALYSIS SET FORTH IN THIS COURT'S OPINION IN *EAST RIVER*.

The task before the Ninth Circuit in *Saratoga Fishing Co. v. Marco Seattle, Inc.*, 69 F.3d 1432 (9th Cir. 1995), was

to determine whether the economic loss rule adopted by this Court in *East River S.S. Corp. v. Transamerica Delaval*, 476 U.S. 858 (1986) applies to the product purchased by the plaintiff, or to an earlier configuration of the product consisting of important components manufactured and supplied by the defendants. Following what is referred to in the case law alternatively as the "benefit of the bargain" rule and the "object of the bargain" test, the Ninth Circuit found that the economic loss rule precluded any claim of Saratoga Fishing Co. – plaintiff below and Petitioner here – in tort for the tuna-seining vessel that Petitioner had purchased, including the seine, skiff, electronic equipment, speed boats, fuel, spare parts and other miscellaneous items that had all been supplied to Petitioner as part of the tuna seiner. Petitioner ("Saratoga")[1] and All Alaskan Seafoods, Inc. ("All Alaskan") challenge the Ninth Circuit's use of the "benefit of the bargain" test.

In *East River*, this Court explained that "[d]amage to a product itself is most naturally understood as a warranty claim," 476 U.S. at 872, because the purchaser has failed to receive the benefit of its bargain. When a product injures itself, it fails to perform according to expectations and the purchaser does not receive the anticipated value from the product purchased. "Such damage means simply that the product has not met the customer's expectations, or, in other words, that the customer has received 'insufficient product value.' . . . The maintenance

[1] As Saratoga is the successor in interest to Manuel Vargas, who purchased the vessel from Joseph Madruga, for ease of reference "Saratoga" or "Petitioner" will always be used.

of product value and quality is precisely the purpose of express and implied warranties." *Id., quoting* J. White and R. Summers, Uniform Commercial Code 406 (2d ed. 1980). The plaintiff should avail itself therefore of contracts or warranties to recover its economic losses. "Obviously, damage to a product itself has certain attributes of a products-liability claim. But the injury suffered – the failure of the product to function properly – is the essence of a warranty action, through which a contracting party can seek to recoup *the benefit of its bargain." Id.* at 867-68 (emphasis added).

The focus in *East River* thus was on the bargain that the plaintiff, as the contracting party, had made and the fact that the plaintiff did not receive the benefits from the product it purchased. "[W]arranty law sufficiently protects *the purchaser* by allowing it to obtain *the benefit of its bargain*. . . . The expectation damages available in warranty for purely economic loss give *a plaintiff the full benefit of its bargain* by compensating for forgone business opportunities." *Id.* at 873 (emphasis added). "Even when the harm to the product itself occurs through an abrupt, accident-like event, the resulting loss due to repair costs, decreased value, and lost profits is *essentially the failure of the purchaser to receive the benefit of its bargain – traditionally the concern of contract law." Id.* at 870 (emphasis added).

The reasoning in *East River* consequently requires a court to look at what the plaintiff's actual bargain was and the product that the plaintiff purchased for purposes of defining the "product" involved. If contract and warranty law apply because the injury suffered by the plaintiff is the failure of the "product" to meet the plaintiff's

expectations, then "the product" – that part of the plaintiff's property that is governed by contract rather than tort law – can only be defined as the product that plaintiff purchased. A plaintiff negotiates warranties against product failure and appropriate price adjustments with respect to the product that it purchases, *not* with respect to a component, product, or version of the product that a former purchaser bought upstream. A previous transaction involving a product that differs from the product the plaintiff in fact bought is irrelevant.

The Ninth Circuit's opinion in *Saratoga Fishing* flows directly from *East River*. In reaching its holding, the Ninth Circuit stated, "We are guided by the policies set forth in *East River*, where the Court stated that the focus of the product should be on the failure of the purchaser to receive the benefit of its bargain. Warranty and contract law are appropriate for this type of situation. Here, the purchaser is Saratoga *and the object of its bargain was the M/V SARATOGA with the components already installed." Saratoga Fishing*, 69 F.3d at 1444 (emphasis added). The Ninth Circuit accordingly held: "The 'product' in this case is the vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items are part of the product and are not recoverable in a tort action as 'other property.' " *Id.* at 1445. This analysis and result closely follow the reasoning and policies of *East River*.

II. THE RULE FOLLOWED BY THE NINTH CIRCUIT IN *SARATOGA FISHING* IS THE SAME RULE ADOPTED BY VIRTUALLY EVERY COURT THAT HAS CONSIDERED THE ISSUE.

Petitioner and All Alaskan contend that the Ninth Circuit's opinion in *Saratoga Fishing* conflicts with the approach taken by the Fifth Circuit. The opposite is true. The Ninth Circuit's opinion is directly derived from the Fifth Circuit's application of the "object of the bargain" analysis. There is a wealth of carefully reasoned case law adopting *East River's* focus on the plaintiff's bargain as the starting point for defining "product" under the economic loss rule. The doctrinal and commercial certainty that has developed under *East River* will be undermined if the Court were to adopt any of the several rules proposed by the Petitioner or All Alaskan.

A. *Saratoga Fishing* Is Identical To The Fifth Circuit's Approach In Cases Such As *Shipco 2295* And *Nicor*.

The seminal Fifth Circuit case is *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987). The Fifth Circuit held that components of a vessel could not be considered "other property" in language strikingly similar to that of the Ninth Circuit's *Saratoga Fishing*:

> In attempting to identify the product, our analysis leads us to ask *what is the object of the contract or bargain that governs the rights of the parties*? The completed vessels were obviously the objects of the contract. [Plaintiff] Shipco did not bargain separately for individual components of each vessel. *We are persuaded that those same vessels that were the object of the contract must be considered 'the product' rather than the individual components that make up the vessels.*

825 F.2d at 928 (footnote omitted) (emphasis added). The Fifth Circuit stated further, "The product in this context means the finished product *bargained for by the buyer* rather than components furnished by a supplier," and "The critical fact that Shipco *bargained for a finished vessel* remains unchanged." *Id.* at 929-30 (emphasis added). The court also observed that its approach is derived from *East River*: "East River teaches that such economic loss for damage *to the product bargained for*, the vessels in this case, cannot be recovered in tort." *Id.* at 929 (emphasis added).

The Fifth Circuit's subsequent opinion in *Nicor Supply Ships Ass'n v. General Motors Corp.*, 876 F.2d 501 (5th Cir. 1989), follows *Shipco 2295*'s "object of the bargain" test and is also entirely consistent with the Ninth Circuit's approach. *Nicor* held that plaintiff could not recover for fire damage to a vessel allegedly caused by a faulty fuel injector and fuel-conditioning system in a main engine. 876 F.2d at 502, 505. It also held that recovery *could* be had for equipment placed on board the vessel by a third party *after* the plaintiff's purchase of the vessel, because such equipment was *not* a part of the plaintiff's bargain. 876 F.2d at 505. The Ninth Circuit thus correctly observed that *Nicor* is not in conflict with its holding in *Saratoga Fishing*:

> In [*Nicor*], the vessel was sold only once. The buyer then time-chartered the vessel to a third-

> party, who installed equipment on the vessel. The court properly focused on the bargain between the buyer and shipbuilder to determine what was the product. . . . The equipment was deemed 'other property.'

Saratoga Fishing, 69 F.3d at 1444.[2]

B. *Saratoga Fishing*'s Application Of The "Object Of The Bargain" Test Is Also Consistent With The Practice In The Other Federal Circuits And The State Courts.

The "object of the plaintiff's bargain" test has been universally adopted. Federal and state courts agree that in determining whether a product has injured only itself or has injured "other property" for purposes of the economic loss rule, the "product" at issue is the integrated product the plaintiff purchased. The Eleventh Circuit has stated the rule concisely and in no uncertain terms: "The

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[2] Other Fifth Circuit cases are to the same effect. In *Petroleum Helicopters, Inc. v. Avco Corp.*, 930 F.2d 389 (5th Cir. 1991), a helicopter was damaged when an emergency floatation device (originally sold to plaintiff with another helicopter) allegedly malfunctioned during a water landing and caused the helicopter to capsize. The Fifth Circuit held that damage to the helicopter constituted economic loss and could not be recovered under a product liability theory against the manufacturer of the float. 930 F.2d at 393. In *American Eagle Ins. Co. v. United Technologies Corp.*, 48 F.3d 142, 145 (5th Cir. 1995) *modified on other grounds on reh'g*, 51 F.3d 468 (5th Cir. 1995), the defendant sold a defective engine to Cessna Caravan Aircraft, which installed it in an aircraft. The aircraft was sold *five times*, the last purchaser being plaintiff Martinaire, Inc. The Fifth Circuit expressly focused on the object of plaintiff Martinaire's bargain, and held that the "product" was the aircraft that Martinaire purchased.

character of loss determines the appropriate remedies, and, to determine the character of a loss, *one must look to the product purchased by the plaintiff, not the product sold by the defendant." Pulte Home Corp. v. Osmose Wood Preserving, Inc.*, 60 F.3d 734, 741 (11th Cir. 1995) (emphasis added) (*quoting Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d 1244, 1247 (Fla. 1993)). The Third Circuit agrees:

> As we read East River, it is the character of the plaintiff's loss that determines the nature of the available remedies. When loss of the benefit of a bargain is the plaintiff's sole loss, the judgment of the Supreme Court was that the undesirable consequences of affording a tort remedy in addition to a contract-based recovery were sufficient to outweigh the limited interest of the plaintiff in having relief beyond that provided by warranty claims. The relevant bargain in this context is that struck by the plaintiff. It is that bargain that determines his or her economic loss and whether he or she has been injured beyond that loss."

King v. Hilton-Davis, 855 F.2d 1047, 1051 (3d Cir. 1988), *cert. denied*, 488 U.S. 1030 (1989). The overwhelming number of federal and state courts that have considered the issue of what constitutes "the product" for purposes of *East River* have employed the "object of the bargain" test and held that "the product" is the product purchased by the plaintiff.[3]

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[3] *See, e.g., Hininger v. Case Corp.*, 23 F.3d 124 (5th Cir. 1994); *American Home Assurance Co. v. Major Tool & Mach., Inc.*, 767 F.2d 446, 447-48 (8th Cir. 1985); *Bowling Green Mun. Utils. v.*

The Petitioner and All Alaskan invite the Court to disregard this body of authority in favor of decisions that predate or fail to follow *East River*. None of the cases cited by Petitioner or All Alaskan announce a rule that supports their arguments, or provide any guidance to the Court in fashioning a rule that would not severely restrict the import of *East River*.[4]

Thomasson Lumber Co., 902 F. Supp. 134, 139 (W.D. Ky. 1995); *Exxon Shipping Co. v. Pacific Resources, Inc.*, 835 F. Supp. 1195, 1200-01 (D. Haw. 1993); *Karshan v. Mattituck Inlet Marina & Shipyard Inc.*, 785 F. Supp. 363, 364 n.1 (E.D.N.Y. 1992); *ERA Helicopters, Inc. v. Bell Helicopter Textron, Inc.*, 696 F. Supp. 1096 (E.D. La. 1987); *Bocre Leasing Corp. v. General Motors Corp.*, 84 N.Y.2d 685, 645 N.E.2d 1195 (1995); *Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d at 1247; *Utah Int'l, Inc. v. Caterpillar Tractor Co.*, 108 N.M. 539, 541-42, 775 P.2d 741, 743-44 (Ct. App.), *cert. denied*, 108 N.M. 354, 772 P.2d 884 (1989).

[4] In some of these cases, as *Nicor* held, the courts merely upheld products liability claims for damage to property or equipment that the plaintiff (subsequent to purchase) added to, combined or used with the "product." *See, e.g., McDermott, Inc. v. Clyde Iron*, 979 F.2d 1068 (5th Cir. 1992) (defective crane purchased by plaintiff and deck being moved by crane both damaged; tort recovery allowed for damage to deck but not to crane); *Mays Towing Co. v. Universal Mach. Co.*, 755 F. Supp. 830 (S.D. Ill. 1990) (plaintiff purchased defective engines and installed them in its river towboat; plaintiff was not able to recover in tort for damage to engines, but could recover for damage to the rest of the vessel). In other cases, the courts' conclusions were controlled by the very state law approaches rejected by *East River*. *See Rosenau v. City of New Brunswick, N.J.*, 51 N.J. 130, 238 A.2d 169 (1968) (permitting recovery for damage to the product itself); *Sacramento Regional Transit Dist. v. Flexible*, 158 Cal. App. 3d 289, 205 Cal. Rptr. 736 (1984) (same); *Kodiak Elec. Ass'n v. Delaval Turbine, Inc.*, 694 P.2d 150, 153-54 (Alaska 1984) (same); *Fordyce Concrete, Inc. v. Mack Trucks, Inc.*, 535 F. Supp. 118, 124-25 (D. Kan. 1982) (same). The remaining cases – those involving asbestos contamination of public buildings and shopping centers – do not counsel abandoning the "object of the bargain" approach. These cases turn on the unique nature both of the "defect" of asbestos and the damage it causes. *See, e.g., Board of Educ. of the City of Chicago v. A, C and S, Inc.*, 131 Ill. 2d 428, 446, 546 N.E.2d 580, 588 (1989). They hold that asbestos actions are a hybrid of economic loss, personal injury, and physical damage to property. *See City of Manchester v. National Gypsum Co.*, 637 F. Supp. 646, 649-50 (D.R.I. 1986); *Northridge Co. v. W.R. Grace & Co.*, 162 Wis.2d 918, 932, 471 N.W.2d 179, 184 (1991); *A, C and S, Inc.*, 546 N.E.2d at 588. These cases accordingly find that the harm suffered by the plaintiffs does not fit within the usual definition of "economic loss" because breakdown of asbestos causes dispersion of a "hazardous," "dangerous" and "highly toxic substance" that is injurious to the occupants and to the public that uses the buildings. *See T.H.S. Northstar Ltd. v. W.R. Grace & Co.*, 767 F. Supp. 969, 973-74 (D. Minn. 1991); *City of Manchester*, 637 F. Supp. at 650-51; *Northridge Co.*, 471 N.W.2d at 184, 186; *A, C and S, Inc.*, 546 N.E.2d at 588, 590.

III. THE "OBJECT OF THE BARGAIN" TEST APPLIED BY THE NINTH CIRCUIT IS FAIR BECAUSE IT PRESERVES THE TERMS OF THE PLAINTIFF'S BARGAIN AND HONORS THE CONTRACTUAL ARRANGEMENTS MADE IN UPSTREAM TRANSACTIONS.

A. It Is Fair To Leave Petitioner To The Terms Of Its Bargain.

Commercial parties to a sale can and are expected to negotiate price and to allocate their respective rights, risks, liabilities, and remedies. A purchaser may obtain extensive warranties and pay more for a product, or it may decide to forego warranties, accept (and perhaps insure) the risk that the product might malfunction, and

obtain a discounted price. Petitioner thus is not left unprotected by the Ninth Circuit's unwillingness to extend tort remedies to some of the vessel's components. Instead, at the time it struck its bargain with Madruga, Petitioner had every opportunity, through warranty or insurance, to protect itself from economic disappointment if the fully outfitted purse seiner failed to perform.

The fairness of holding commercial parties to their bargains is one of the fundamental premises of *East River*. "Contract law, and the law of warranty in particular, is well suited to commercial controversies of the sort involved in this case because the parties may set the terms of their own agreements. The manufacturer can restrict its liability, within limits, by disclaiming warranties or limiting remedies. . . . In exchange, the purchaser pays less for the product. Since a commercial situation generally does not involve large disparities in bargaining power, . . . we see no reason to intrude in the parties' allocation of the risk." 476 U.S. at 872-73. The Court accordingly stated that "[t]here is no reason to extricate the parties from their bargain." *Id.* at 875.[5]

[5] Courts applying the economic loss rule have made similar observations. The Eleventh Circuit in *Pulte Home Corp.* stated: "The rationale underlying the economic loss rule is that parties should protect against the risk of economic loss during contract negotiations through warranty provisions and price adjustments rather than attempt to recovery under tort law after the loss occurs." 60 F.3d at 739-40. *See also Detroit Edison Co. v. Nabco, Inc.*, 35 F.3d 236, 240 (6th Cir. 1994): "The rationale behind this definition of economic loss is that losses based on damage to the product itself are the sort of losses that can and should be addressed by the parties in negotiating the conditions and specifications of a sale.

By defining "the product" to include the components Madruga added to transform the P/V Saratoga into an operational tuna seiner, the Ninth Circuit kept Petitioner to the terms of its bargain as *East River* requires. Any definition of "the product" that looks to an earlier sale would "extricate" commercial parties from their bargains. If a plaintiff can reach upstream and sue a manufacturer in products liability when the product it purchased fails, that plaintiff receives not only the benefit of the lower price it negotiated but also a supplement to its reasonable economic expectations in the form of products liability remedies against a manufacturer. Because it is reasonable to hold commercial parties to their bargains, however, courts have focused on the *plaintiff's* bargain and have refused to permit this "supplement." *See, e.g., Pulte Home Corp.*, 60 F.3d at 742 ("Having failed to avail itself of the opportunity to mitigate the risks of potential disappointment at the time of contract negotiation, [plaintiff] cannot now resort to the courts to save it from a bargain improvidently made").

B. The "Object Of The Bargain" Test Protects The Contractual Arrangements That Had Been Negotiated Upstream From Plaintiff's Bargain.

The commercial realities observed by the Supreme Court in *East River* also apply in upstream transactions during production of the product purchased by the plaintiff. Manufacturers selling components to be used in complex products such as a tuna seiner make contracts with

each other, third parties, and purchasers with regard to the risks and liabilities associated with fabricating the completed product. In each instance, such manufacturers set their price, and have the opportunity to negotiate warranties and impose limitations on their liability for the economic consequences if their components fail.

Contractual arrangements that limit liability for property damage and related losses – either in tort or warranty – are valid in a commercial context.[6] It is perfectly natural for a supplier, presumably in exchange for a lower profit, to disclaim liability for losses that may arise in a commercial endeavor. The economic loss rule respects these upstream transactions by permitting only contract and warranty remedies in commercial controversies that arise when products fail to operate properly.

Although valid between suppliers and buyers of components to be used in ultimate products, and between sellers and buyers of finished products, liability limitations are difficult to impose on remote purchasers.[7] Tort liability may be even more difficult to contain effectively

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[6] *East River*, 476 U.S. at 873 n.8 (citing *Keystone Aeronautics Corp. v. R.J. Enstrom Corp.*, 499 F.2d 146, 149 (3d Cir. 1974)); *Agip Petroleum Co. v. Gulf Island Fabrication, Inc.*, 920 F. Supp. 1330, 1341 (S.D. Tex. 1996) ("Under admiralty law, clauses limiting liability for negligence and strict liability are valid and enforceable." [citing *Nicor*]) This also is the rule in land-based cases. *See, e.g., McDermott*, 979 F.2d at 1076; *Idaho Power Co. v. Westinghouse Elec. Corp.*, 596 F.2d 924 (9th Cir. 1979).

[7] *Hininger*, 23 F.3d at 124, *citing Patty Precision Products Co. v. Brown & Sharpe Mfg Co.*, 846 F.2d 1247, 1257 (10th Cir. 1988) ("it may be difficult or even impossible for a component manufacturer to disclaim its warranty liability") .

with contractual arrangements. *King*, 855 F.2d at 1050. Were it not for the economic loss rule, these difficulties in limiting liability to downstream purchasers would expose component suppliers to uncertain and far-reaching liability. Because contractual limitations of liability are difficult to impose except on direct purchasers, any resale of a component – even before it was integrated into a finished product – would transform a commercial relationship with fixed allocation of risks and remedies into an inquiry about public duties, product defect and limitless economic consequences. *See East River*, 476 U.S. at 874.

The plaintiff's bargain is the appropriate place to start in defining the "product" because, that is the transaction where the plaintiff has an opportunity to fix its own economic expectations regarding the product it is purchasing. Defining the product on the basis of any upstream transaction (such as Madruga's purchase of some parts of the tuna seiner) carries with it the likelihood of nullifying the commercial arrangements of upstream participants in the supply chain. If the "product" does not change as new components are added to it, or it is modified, the economic loss rule loses touch with the plaintiffs' bargain and exposes suppliers to liability for downstream commercial expectations, however they may have tried to control their liability when selling their products or components.[8]

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[8] *See Bocre Leasing Corp.*, 84 N.Y.2d at 693, 645 N.E.2d at 1199, a thoughtful decision by the New York Court of Appeal explaining its adoption of the economic loss rule and its focus on the plaintiff's bargain.

"Given the reality of already existing, ample deterrents to manufacturers injecting unsafe products into the commerce

Courts, accordingly, have refused invitations to define "products" on the basis of upstream transactions. *King*, 855 F.2d at 1054 ("Implicit in the [economic loss rule] is the policy judgment that in a commercial context the possibility of an inadequate recovery . . . does not justify permitting a tort recovery that will allow a purchaser to reach back up the production and distribution chain, thereby disrupting the risk allocations that have been worked out in the transactions comprising that chain"); *Hininger*, 23 F.3d at 127; (same). *Saratoga Fishing*, by ruling that the "product" was defined by the plaintiff's bargain merely adopted the reasoning of these courts, extracted directly from *East River*, that it was

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stream, and the resultant lack of a substantive public policy purpose to be furthered by imposing additional tort liability in these circumstances, no tort recovery can be had against the manufacturer for contractually based economic loss, whether due to injury to the product itself or consequential losses flowing therefrom. . . .

Tort recovery in strict products liability and negligence against a manufacturer should not be available to a downstream purchaser where the claimed losses flow from damage to the property that is the subject of the contract. Transforming manufacturers into insurers, with the empty promise that they can guarantee perpetual and total public safety, by making them liable in tort for all commercial setbacks and adversities is not prudent or sound tort public policy. In such instances, no directly related or commensurate public interest is served or protected by holding manufacturers liable. Tort law should not be bent so far out of its traditional progressive path and discipline by allowing tort lawsuits where the claims at issue are, fundamentally and in all relevant respects, essentially contractual, product-failure controversies. Tort law is not the answer for this kind of loss of commercial bargain."

unfair to disrupt an entire chain of commercial arrangements in order to augment the plaintiffs' available remedies for its own commercial disappointment.[9]

In recognition of the same values that yielded the *East River* decision, the Court should affirm the Ninth Circuit's application of the "object of the bargain" test. It differentiates between the "product" and "other property" in a way that conforms to commercial expectations and protects the ability of all parties to strike meaningful bargains. There is no reason to prefer – and, in fact, every reason to subordinate – the plaintiff's ability to recover in tort to the attempts by upstream suppliers to control their liability. After all, the plaintiff had an opportunity at the time of purchase to protect against economic disappointment.

C. The Ninth Circuit's Benefit Of The Bargain Approach "maintain[s] a realistic limitation on damages."

This Court declared in *East River* that in addition to keeping products liability and contract law in separate

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[9] Petitioners and All Alaskan complain that the Ninth Circuit's application of the "object of the bargain" test is unfair because recovery for the components added to the vessel by Madruga then depends on "bad luck" that the product failed after it was purchased. First, plaintiff's recovery depends not on luck, but on how it has chosen to arrange its commercial risks when striking its bargain. Second, the "bad luck" is far more likely to fall on the suppliers of components. If Petitioner's views were adopted, such suppliers' attempts to control liability through contractual arrangements will be scuttled by fortuitous resale of their products to a remote purchaser with whom they have no contract or opportunity to negotiate.

spheres, it adopted the economic loss rule out of a concern "to maintain a realistic limitations on damages." 476 U.S. at 871. The Court observed, "A warranty action also has a built-in limitation on liability, whereas a tort action could subject the manufacturer to damages of an indefinite amount." *Id.* at 874. It explained further:

> In products-liability law, where there is a duty to the public generally, foreseeability is an inadequate brake. . . . Permitting recovery for all foreseeable claims for purely economic loss could make a manufacturer liable for vast sums. *It would be difficult for a manufacturer to take into account the expectations of persons downstream who may encounter its product.* In this case, for example, if the charterers – *already one step removed from the transaction* – were permitted to recover their economic losses, then the companies that subchartered the ships might claim their economic losses from the delays, and the charterers' customers might also claim their economic losses, and so on. 'The law does not spread its protection so far.' "

Id. (citations omitted).

Petitioner's and All Alaskan's proposal that the first sale of a product by the manufacturer determine the "product" for all transactions downstream disregards the concern for putting a limit on damages downstream. Their approach subjects manufacturers to liability for all alterations to, modifications or updating of, or repairs to the product by all purchasers subsequent to the original sale. If products are used in the "modification" of a vessel, Petitioner and All Alaskan would make the manufacturer, even of the most trivial component, liable for all

lost profits associated with the use of the "original" product. The Ninth Circuit's ruling in *Saratoga Fishing* and implements this Court's directive to avoid such limitless economic exposures.

IV. PETITIONER AND ALL ALASKAN FAIL TO PROPOSE A RULE FOR DECISION THAT SQUARES WITH *EAST RIVER*.

Petitioner and All Alaskan suggest that the Ninth Circuit should have applied any number of "rules" which would make tort remedies available against these defendants. What undermines all of their approaches is that *East River* already has reconciled the restriction of tort remedies with the advantages of applying contract law to economic losses. Petitioner's and All Alaskan's artificial attempts to segregate *East River's* discussion of contract law from its products liability analysis reflects a fundamental misunderstanding of the decision – a misunderstanding that is at the heart of every challenge they make to the Ninth Circuit's ruling.[10]

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[10] Petitioner and All Alaskan claim that *East River* contains two separate and independent discussions, the first an analysis of products liability law, followed by a discussion of warranty laws. Petitioner's brief at 19-24; All Alaskan's brief at 9-12. This Court knows best what it intended, but it appears quite plain from the opinion and it certainly has been the reaction of the judiciary that *East River* defined economic losses from the perspective of the plaintiff's bargain. The decision simultaneously considered tort and contract law, and determined that warranty law more appropriately addressed the failure of a product to meet a plaintiff's expectations – or, as the Court put it, "the failure of the purchaser to receive the benefit of its bargain," 476 U.S. at 870.

A. Arguments That A Product Is Any Physically Distinct Article That A Seller Places In Commerce Ignore The Premises Of *East River*.

Petitioner and All Alaskan analyze the issue of what constitutes "the product" exclusively from the point of view of the manufacturer of the defective product rather than of the bargain struck by the plaintiff. They insist again and again that "the product" must be defined by the defective product the manufacturer has placed on the market. *See* Petitioner's brief ("Pet. Br.") at 3-4 ("the product in products liability cases, including maritime products liability cases, is determined by what the *manufacturer* places in the stream of commerce"); All Alaskan's brief ("All Al. Br.") at 4 ("the appropriate focus must be on the *original manufacturer* and its sale to the *initial user*") and 16 ("the product" must be defined "through the eyes of the manufacturer") (emphasis added) *See also* Pet. Br. at 8, 9, 12, 18, 24, 27, 29, 34-35; All Al. Br. at 2, 7 n.3, 13, 20-21.[11]

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[11] As support for these broad statements, Petitioner and All Alaskan offer a single remark in the *East River* opinion supposedly showing that the manufacturer's sale rather than the plaintiff's bargain was the focus of the Court's concern. Because the Court observed that "[s]ince each turbine was supplied by Delaval as an integrated package, . . . each is properly regarded as a single unit," 476 U.S. at 867, Petitioner and All Alaskan claim that this Court was asserting a rule that "the product" must be defined as that product "supplied by the manufacturer." *See, e.g.*, Pet. Br. at 21; All Al. Br. at 10-11. The Court's comment that each turbine was properly regarded as a single unit was offered in the context of the Court's *rejection* of the theory that one component could damage another. *See* 476 U.S. at 867. The Court was not addressing the issue of whether any other component *of the vessels* might or might not be considered part of the product. Because no other component of the vessels was harmed, the Court did not have to discuss that issue.

Petitioner struggles a bit itself with the breadth of its argument when it acknowledges that – under both *Shipco 2295* and *Nicor* – harm to any or all components of a vessel which is the object of the plaintiff's bargain is immune to a tort theory. Pet. Br. at 29-30. To avoid application of this rule here, Petitioner argues that the "skiff, net, fuel, spare parts, speed boats and miscellaneous equipment added to M/V SARATOGA . . . are physically distinct individual products in their own right. . . . " *Id.* at 31. This characterization of the equipment, however, fails to advance the discussion at all. A fully outfitted tuna seiner is as capable of being called a "physically distinct product in its own right" as a partially outfitted vessel. Surely the vessels in *Nicor* and *Shipco 2295* employed components that might be called physically distinct. Yet the courts in those cases analyzed the "product" in terms of the plaintiff's bargain, not by when "physically distinct" elements were added to the vessel.

Petitioner and All Alaskan also argue that, unless the product is defined by the manufacturer's sale of the article, the public policy of strict products liability will be compromised. They suggest that holding a manufacturer accountable in tort will "establish parameters of accountability," will protect the downstream consuming public, will attribute "blame on those who are best suited to

prevent injury or damage due to dangerous and defective products, the product manufacturers," and that the "end result . . . will be that products will be safer." *See* Pet. Br. at 17-19; All Al. Br. at 14. Again, these considerations were part of the Court's calculus in *East River*. The Court determined that these tort law policies were weak and warranty law was primary when a product purchased by the plaintiff damages itself and causes economic loss. 476 U.S. at 871. It makes no sense, then, to turn to tort policies when determining how "the product" should be defined.

Finally, Petitioner and All Alaskan vigorously argue that the stability of maritime law is threatened by the benefit of the bargain analysis applied by the Ninth Circuit. The court's analysis, however, already has stood the test of many maritime and land-based judicial decisions and offers an objective, fair and certain measurement of "the product" that conforms to accepted commercial realities. The approach offered by Petitioner and All Alaskan, to the contrary, is arbitrary and impossible to implement. Although it is clear that Petitioner would prefer to measure the product from the Martinac/Madruga transaction in this case[12], it is wholly unclear how a future case

[12] *See* Pet. Br. at 12-13. Petitioner suggests that Madruga was the "first" or "original" buyer. This is circular reasoning. For example, if the "product" were the hydraulic system that malfunctioned aboard the M/V SARATOGA, Martinac – who purchased it from Marco – would be the "first" buyer. Conversely, if the product is the fully outfitted purse seiner, Madruga – who purchased all of the components and assembled them to his specifications – would be the first buyer. In other words, unless the product already has been defined, it is impossible to identify the "first buyer."

would be resolved. It is difficult to imagine how courts will distinguish between components and products when the rule proposed calls for entire ships to be the "product" on the one hand, but – with only the fact that they must have been sold by a manufacturer as guidance – for partially outfitted tuna seiners to be the "product" on the other.[13]

B. The "Static" Product Argument Ignores Commercial Realities And The Premises Of *East River*.

Petitioner argues that the Ninth Circuit erred by asking whether the product "changed" when Madruga completed outfitting of the vessel. Pet. Br. at 22-23. All Alaskan, similarly argues that a downstream purchaser cannot "remanufacture" a product placed on the market by an initial manufacturer. All Al. Br. at 21-24. Both argue that, since Madruga added components to the vessel *after* his bargain with Martinac, Respondents would have been liable in tort for this "other property" but for the "fortuity" or "pure luck" of a resale to Saratoga. Pet. Br. at 32-33; All Al. Br. at 23-25. Both claim the Ninth Circuit

[13] It is even more difficult to conceive how All Alaskan would have this Court distinguish between a manufacturer's "components" and its "products." The item at issue in its case with Raychem – an electrical heating cable – is a small, inexpensive wiring product that was physically integrated into the vessel. Any workable rule of law that purports to implement *East River*, *Shipco 2295*, and *Nicor* must account for the differences between such components of the vessel and the vessel itself.

decision thus poses a problem of "vanishing" tort liability. *Id.*

There are at least three defects in this reasoning. First, a resale (particularly of a significantly changed product) is not a fortuitous or chance event. It is a commercial transaction in which the purchaser has the opportunity to control its economic risks. Petitioner concedes that it is common for vessels to be outfitted for a particular purpose and resold. Pet. Br. at 9-10. Just using the facts of the *Saratoga Fishing* and *All Alaskan v. Raychem* as examples, in both cases the owner/user of the vessel made substantial, commercial changes to the vessels. In *Saratoga Fishing*, Madruga contracted with other vendors after he took title to the vessel to complete outfitting it for tuna fishing, always its intended purpose. In *All Alaskan v. Raychem*, the seller of the vessel contracted with a shipyard to convert its vessel (once a military vessel) to a salmon processor. Both of these sellers added components, large and small, to the vessel with the help of experienced shipyards and suppliers. When the buyers of those vessels bargained for them, they had already been outfitted for their intended purposes. It makes little sense and certainly depends on fortuity to say that the very modifications to the vessel that make it what it is are not part of the product because they happened to occur after a fishing company took title to the vessel.

Second, *East River* already makes it plain that tort liability may change as components and products change hands. By definition, if the economic loss rule has any vitality, it must protect component manufacturers from tort liability for losses arising if the component damages

the ultimate product.[14] Before the component is integrated into the product and sold, however, the manufacturer may well have – absent a contractual disclaimer – a tort remedy if the component damages other property.[15] After the component is integrated into the product and sold, however, *East River* has already determined that there is no tort recovery available for harm to the (new) product itself from the manufacturer *or* the component manufacturer.

Last, the products liability that Petitioner and All Alaskan posit has "vanished" may well not exist in the first place. Because the supplier may have contracted to limit its tort liability with the "original" buyer, tort liability – if the Ninth Circuit's approach is rejected – may "spring" into being rather than "back to zero" upon a resale. The fact is that Petitioner and All Alaskan are talking about two very different activities when they compare potential tort liability to Madruga for the equipment he added versus potential tort liability to Saratoga for loss of the purse seiner. In the first, Martinac and Marco had an opportunity to allocate risks among themselves and Madruga including for equipment he added to

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[14] In *East River*, quoting *Northern Power & Eng'g Corp. v. Caterpillar Tractor Co.*, 623 P.2d 324, 330 (Alaska 1981), the Court observed, " 'Since all but the very simplest of machines have component parts, [a contrary] holding would require a finding of 'property damage' in virtually every case where a product damages itself. Such a holding would eliminate the distinction between warranty and strict liability.' " 476 U.S. at 867.

[15] This is essentially the holding in *Nicor* where "other property" added to that which formed the plaintiff's bargain was recoverable in tort.

the vessel. In the second, Saratoga Fishing had every opportunity to protect against economic losses caused by the performance of the product it purchased, the fully outfitted purse seiner. *East River* makes it clear that it is appropriate to treat these transactions differently.

C. Whether Or Not A Seller Is A "Restatement Section 402A Seller" Is Irrelevant To This Court's Analysis In *East River*.

Petitioner has proposed one more test to determine "the product" that is found in neither *East River* nor the case law concerning the economic loss rule. According to Petitioner, "the product" is that which is sold by a seller who fits within section 402A of the Restatement (Second) or Torts. Pet. Br. at 28. Conversely, Petitioner proposes that a transaction involving a non-402A seller cannot be the transaction that determines what "the product" is, even if it is the transaction in which the plaintiff made its purchase. *Id.* at 28. In keeping with its proposed "test," Petitioner goes to great lengths to argue that Madruga, the person who sold the seining vessel to Petitioner, was "a consumer" and an "occasional seller," and was not a 402A seller. *Id.* at 13, 14, 16. *See also* All Al. Br. at 19-21.[16]

Section 402A, however, is entirely irrelevant to this Court's analysis in *East River*. There is no discussion

[16] In making this argument, Petitioner improperly draws factual conclusions about Madruga's status as a 402A seller on the basis of issues that were never litigated before the District Court and of "facts" that were never the subject of any findings by the Court.

concerning and no determination made whether any of the sellers, owners, or charterers involved are 402A sellers. Indeed, *there is no meaningful discussion of section 402A in all of East River*. Section 402A is only mentioned twice in passing, once parenthetically to indicate that one of the Courts of Appeals adopted section 402A in applying strict liability law in admiralty, and once to observe *that section 402A does not answer the question before the Court*. 476 U.S. at 865, 868 n.3. In addition, *no other court following East River or applying the economic loss rule has analyzed or even mentioned whether a 402A seller was involved in the sale of the "product" subject to the economic loss rule.*[17] Section 402A by its express terms does not address the issue presented to the Ninth Circuit in *Saratoga Fishing*. It contains the following caveat: "The Institute expresses no opinion as to whether the rules stated in this Section may not apply . . . to the seller of a component part of a product to be assembled."

[17] *American Eagle Ins.*, in particular, establishes that a seller's status under § 402A has nothing to do with the definition of "the producer." After Cessna purchased and installed the engine in an aircraft, it sold the aircraft to Federal Express Corporation, which presumably does not engage in the business of selling aircraft as required by § 402A(1)(a). *See American Eagle Ins.*, 48 F.3d at 143-44. The aircraft was then sold *four more times* after Federal Express purchased it. The Fifth Circuit, however, did not analyze whether any of the aircraft's purchasers were § 402A sellers. Rather, the Fifth Circuit focused solely on the aircraft as the object of the bargain of *plaintiff*, the fifth and last purchaser.

Under Petitioner's proposed rule, the economic loss rule simply "vanishes" with respect to any components that happen to be installed and integrated into products by "occasional" sellers. Madruga, if he were found to be an occasional seller, would not be liable in strict liability for the hull *or* the equipment he added. His status therefore, does not contribute anything to Petitioner's argument that damage to some components of the purse seiner are governed by tort law while other losses are recoverable only in contract. Section 402A, after all, is intended to determine *who* is responsible if there is any products liability, not *whether* there is liability in the first place. Petitioner's proposed "test" based on a seller's status under § 402A is irrational and must be rejected.

V. CONCLUSION

The Ninth Circuit applied the rationale of *East River* to reach a fair result that is consonant with the approach taken by every Federal court to consider the issue. The National Association of Manufacturers and Raychem Corporation respectfully urge the Court to affirm the Ninth Circuit's ruling with regard to the equipment added by

Madruga to fully outfit the M/V SARATOGA before it was sold to Petitioner for tuna fishing.

Respectfully submitted,

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